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Cover Page Footnote

Professor of Law, Fordham University School of Law. This article is adapted from a study prepared by Professor Kessler for the New York State Law Revision Commission.

THE NEW UNIFORM LIMITED PARTNERSHIP ACT: A CRITIQUE

ROBERT A. KESSLER*

INTRODUCTION

THE limited partnership was one of America's early European imports.¹ In this business form, at least one person must have unlimited liability for the business obligations of the entity, but all other partners can, as in the modern corporation, have their liability limited to their agreed contribution.² New York is credited with having enacted the first American statute authorizing the limited partnership.³ Other states soon followed New York, and, in 1916, the National Conference of Commissioners on Uniform State Laws, whose function is to "promote uniformity in [state laws] on subjects where uniformity is desirable and practicable,"⁴ proposed the Uniform Limited Partnership Act (ULPA), which was subsequently enacted in every state except Louisiana.⁵

In 1976, less than four years after the latest adoption of the ULPA,⁶ the Commissioners promulgated a Revised Uniform Limited Partnership Act. Developments during 1979 have lent added urgency to the need to consider the effect which adoption of the new Act will have on the state of limited partnership law. At present, three states have already adopted the new ULPA.⁷ Furthermore, the Internal Revenue

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1. H. Reuschlein & W. Gregory, *Handbook on the Law of Agency and Partnership* § 264, at 434 n.54 (1979); 2 S. Rowley, *Partnership* § 53.0, at 550 (2d ed. R. Rowley & D. Sive 1960).

2. See generally J. Crane & A. Bromberg, *Law of Partnership* § 26 (1968); H. Henn, *Handbook of the Law of Corporations* §§ 28-36 (2d ed. 1970); H. Reuschlein & W. Gregory, *supra* note 1, § 264; *Symposium: Limited Partnership Act*, 9 St. Mary's L.J. 441 (1978).

3. Act of Apr. 17, 1822, ch. 244, 1822 N.Y. Laws 259.

4. Constitution of the National Conference of Commissioners on Uniform State Laws, art. 1, § 1.2, *reprinted in* *Handbook of the National Conference of Commissioners on Uniform State Laws* 270 (1978).

5. See 6 Uniform Laws Annotated 93 (Supp. 1979), *Uniform Limited Partnership Act* (1916) [hereinafter cited as ULPA (1916)], Table of Jurisdictions Wherein Act Has Been Adopted.

6. Delaware was the last state to adopt the ULPA (1916). Act of June 25, 1973, ch. 105, 59 Del. Laws 192 (codified at Del. Code Ann. tit. 6, §§ 1701-33 (1974)).

7. Act of Mar. 29, 1979, no. 657, 1979 Ark. Acts ____ (codified at Ark. Stat. Ann. §§ 65-501 to -566 (Supp. 1979)); Act of June 14, 1979, Pub. Act No. 79-440, 1979 Conn. Legis. Serv. 1148 (West) (to be codified at Conn. Gen. Stat. Ann. §§ 34-9 to -37 (West)); Act of Mar. 6, 1979, ch. 153, §§ 17-14-201 to -1104, 1979 Wyo. Sess. Laws 357. The Arkansas law provides in §§ 65-564, -566 that the new Act governs limited partnerships formed after the effective date of the new Act, while the old Act will continue to apply to limited partnerships formed previously, unless the older partnerships elect to file a certificate under the new Act. Section 60 of the Connecticut enactment provides that limited partnerships formed prior to the effective date of the new Act continue to be governed by the old Act, except that such partnerships cannot be renewed unless

Service has tentatively stated that limited partnerships formed under the new Act should receive tax treatment virtually identical to that afforded partnerships formed under the old Act.⁸

This article briefly considers the differences between the old and the new Uniform Limited Partnership Acts, and offers a critique of the latter. Although the new Act is structured in a logical order which serves as a framework for this discussion, the interrelationship of certain articles of the new Act has dictated a topical, rather than a section-by-section, analysis.

I. CORPORATE LAW INFLUENCE

The limited partnership has always been a business alternative to the corporation. Because a majority of states now allow a corporation to be a general partner,⁹ the combined limited liability of the limited partners and the corporate general partner has rendered the limited partnership the functional equivalent of a corporation.¹⁰ An assimilation of certain features of the corporation law into the limited partnership statutes is desirable, therefore, for simplicity as well as for consistency of treatment.

renewal is provided for in the original agreement. The Wyoming statute is silent as to which law will apply.

8. For a discussion of the characteristics which the IRS will consider in determining whether a limited partnership should be classified as an "association," and therefore taxed as a corporation, see Haims & Strock, *Federal Income Tax Classification of Limited Partnerships Formed Under the Revised Uniform Limited Partnership Act*, 9 St. Mary's L.J. 489, 505 (1978). When the new Act was initially promulgated, there was concern as to whether the "safe harbor" provisions, see notes 38-42 *infra* and accompanying text, risked such "centralization of management" as to lead to the taxation of limited partnerships formed under the new Act as corporations. Section 303(b)(5)(v) of the new Act, specifying that a limited partner's exercise of his right to vote on the removal of a general partner would not be construed as an act of control, was particularly suspect. Recently, Rev. Rul. 79-106, 1979-12 I.R.B. 21, has indicated that voting on such matter should not be an additional factor in tax classification, and thus reaffirmed the IRS acquiescence in the interpretation of Treas. Reg. § 301.7701-2(a)(1) (1960) found in *Larson v. Commissioner*, 66 T.C. 159 (1976), *acq.*, 1979-12 I.R.B. 6, under which it is virtually impossible for a limited partnership formed under the old ULPA to be taxed as a corporation. Forthcoming regulations will indicate that limited partnerships formed under the 1916 and the 1976 Uniform Limited Partnership Acts should be treated identically for tax classification purposes. Telephone Interview with National Conference of Commissioners on Uniform State Laws (Sept. 17, 1979).

9. *E.g.*, Conn. Gen. Stat. Ann. § 33-291(e)(4) (West 1960); N.J. Stat. Ann. § 14A:3-1(1)(m) (West 1969); N.Y. Bus. Corp. Law § 202(a)(15) (McKinney 1963); Ohio Rev. Code Ann. § 1701.13(F)(4) (Page 1978); Pa. Stat. Ann. tit. 15, § 1302(18) (Purdon 1967).

10. When a corporation is the sole general partner, the limited partners have a status analogous to that of non-voting corporate shareholders. Although widely used as "tax shelters," at least until the Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520 (1976), see Note, *Tax Classification of Limited Partnerships*, 90 Harv. L. Rev. 745, 760-62 (1977), and the Revenue Act of 1978, Pub. L. No. 95-600, 92 Stat. 2763 (1978), the potential of the limited partnership as an ordinary business vehicle, with the same effective limited liability as a close corporation but with greater flexibility of operation, has not been fully realized.

Accordingly, one of the most striking features of the new Act is the extent to which it has borrowed from corporate law concepts. The new ULPA sets forth name requirements,¹¹ a name reservation provision,¹² a requirement for a registered agent,¹³ a recordkeeping requirement like that of a corporate stock book,¹⁴ and a central filing provision.¹⁵ In addition, the new Act contains an article on foreign limited partnerships and their registration,¹⁶ similar to statutes governing qualification of foreign corporations, and an article on derivative actions.¹⁷

While such correspondence with the corporate law is generally beneficial, the value of such symmetry depends on the degree of similarity between the corporate and limited partnership provisions. Unfortunately, there is no uniform corporation law which coincides with the new Uniform Limited Partnership Act. The closest analogue is the Model Business Corporation Act, which, although influential, has not been adopted in the most significant of corporate jurisdictions—Delaware, New York, and California. Even in the numerous jurisdictions which follow the Model Act, it has usually been extensively modified: a model act, unlike a uniform act, carries an implied invitation to selective adoption and modification of its provisions.¹⁸

Because of the divergence between the corporation statutes of the various states, it is impossible to fashion a limited partnership act with provisions which correspond to the corporate law of each jurisdiction. The inevitable result is the necessity for numerous changes in the language and the substance of the new Act to produce the necessary correlation in each state adopting the new ULPA. By adopting so many corporate analogues in the new ULPA, the Commissioners seem to presuppose the desirability of such symmetry. The impossibility of achieving complete congruence without extensive amendment to either the state's corporation law or to the Uniform Act, which would destroy its "uniform" character, is a major objection to the new Act.

II. FORMALITIES OF ORGANIZATION

Unlike a general partnership, the formation of a limited partnership is dependent upon compliance with statutory formalities.¹⁹ The new

11. Revised Uniform Limited Partnership Act § 102 (1976) [hereinafter cited by section or article number only].

12. § 103.

13. § 104.

14. § 105.

15. § 206.

16. Art. 9.

17. Art. 10.

18. Furthermore, the ABA committee which drafted the Model Act has been so active in proposing amendments to it that it has become virtually impossible for legislators to keep up with the latest version.

19. H. Henn, *supra* note 2, § 29, at 67.

Act carries over from the old Act the requirement that a limited partnership certificate be filed.²⁰ There is some ambiguity in the statute, however, as to the purpose of the certificate. According to the Comment to section 201 of the new Act:

[T]he certificate is intended to serve two functions: first, to place creditors on notice of the facts concerning the capital of the partnership and the rules regarding additional contributions to and withdrawals from the partnership; second, to clearly delineate the time at which persons become general partners and limited partners.²¹

Yet the avowed first purpose of the certificate—notice to creditors of capital and contributions—conflicts with section 208, which provides that the certificate is notice that “the partnership is a limited partnership and the persons designated therein as limited partners are limited partners, *but it is not notice of any other fact.*”²² Arguably, the fundamental purpose of the certificate is, as the section states, simply to inform third parties of the risks they take in dealing with a limited partnership. This purpose is adequately served, however, by the provision of the new Act which requires the name of the business to include the words “limited partnership.”²³ There is no reason to assume that persons dealing with a limited partnership, identified as such, are less sophisticated than those dealing with a corporation. Furthermore, if the certificate serves only as notice of the partnership’s limited liability, the requirement of section 202(b) that the certificate be promptly amended upon any change in the amount or character of contributions seems clearly superfluous.

Therefore, it seems that the certificate is designed, as the quoted Comment states, to provide more information than mere notice of limited liability. The names and business addresses of the general partners, required by section 201, are valuable items of information for creditors, since the general partners are ultimately liable for the partnership obligations.²⁴ Although the new Act requires it,²⁵ there is,

20. Compare § 201 with ULPA § 2 (1916).

21. § 201, Comment. It is unclear how § 201(b), which provides that the limited partnership begins when the certificate is filed, or at a later time specified therein, accomplishes the aim of delineating the time at which persons become partners. Presumably, the Comment is also alluding to § 202’s requirement of amendment of the certificate within 30 days to reflect the admission or withdrawal of a limited partner.

22. § 208 (emphasis added).

23. § 102.

24. Obviously, any change in the information regarding the partners, especially the withdrawal of a general partner, should result in amendment of the certificate. The simplest way of insuring such amendment is to put the burden on the withdrawing partner to amend the certificate on pain of continued personal liability until such change is made. In contrast, § 202(c) places liability for failure to amend on the remaining general partners, possibly because a failure to amend could be construed as a misrepresentation on their part.

25. § 201(a)(4).

however, no real need to set forth any such information about the partners who have only limited liability,²⁶ any more than there is a need to compel the disclosure of the names of a corporation's shareholders to the corporation's creditors. If any additional information on financial matters is desirable, it could well be limited to the total amount of the limited partners' contributions and their right to withdraw from the partnership.²⁷ Such disclosure would give creditors information on the total minimum capitalization of the partnership as a guide to the amount of credit which could be extended without relying on the personal liability of the general partners.

On the other hand, a fully detailed certificate might aid the partnership by obviating the need for a separate partnership agreement; in fact, the new Act could have expressly permitted the certificate to include the full partnership agreement, just as the certificate of incorporation may include shareholder agreements under some corporate statutes.²⁸ But even if that section of the new Act which allows insertion in the partnership certificate of "any other matters the partners determine to include therein"²⁹ were to be broadly interpreted to permit inclusion of the entire partnership agreement, few attorneys would do so, because of the prompt amendment requirements and liability provisions of the new ULPA. The new Act permits a party injured by a false statement in the certificate to recover damages, and, therefore, provides an inducement to keep certificate provisions to a minimum. Because a statement may be rendered false by reason of the fact that "any arrangement or other fact described in the certificate has changed, making the statement inaccurate in any respect,"³⁰ certificate provisions could become a fertile source of litigation. A wise alternative might be to require lawyers to draft an express written agreement³¹ in order to reduce certificate provisions to a minimum.³²

26. In this regard, it would be advisable to prohibit the use of the name of a limited partner in the firm name, rather than risk creditor misapprehension by allowing its use under the exemption set forth in § 102(2).

27. Apparently in keeping with this approach, § 201 does not carry over the requirement of ULPA § 2(1)(a)(ix), (xii) that the profit shares and priorities of the limited partners be stated in the certificate.

28. *E.g.*, Me. Rev. Stat. Ann. tit. 13-A, § 618 (1964); S.C. Code § 33-11-220 (1976).

29. § 201(a)(13).

30. § 207(2). This section omits reference to the thirty-day grace period, provided by § 202(b), during which the partnership must amend the certificate to reflect any change in financial matters. Presumably, the period must be read into § 207(2). It is unclear, however, when the grace period begins to run.

31. Under § 101(9), a partnership agreement may be written or oral.

32. Additionally, the new Act expressly requires the filing of the limited partnership certificate with the respective secretary of state. § 206. Formerly, the location of the filing office was left to the state's discretion. New York law currently mandates filing with the local county clerk. N.Y. Partnership Law § 91(b) (McKinney 1948). Many other states have the same requirement. *See* J. Crane & A. Bromberg, *supra* note 2, § 26, at 145-46. Because the new Act also forbids the limited

Although the framers of the new Act purport to recognize the partnership agreement as the basic document in any partnership,³³ their treatment of the partnership certificate has worked an unfortunate compromise between the philosophy of full incorporation of all vital matters and that of mere notice to protect creditors, thereby perpetuating the ambiguity of the old Act.³⁴ Both a partnership agreement and a detailed certificate are, in effect, necessary, but neither is sufficient. The certificate, however, especially because of the vagueness of the changes mandated by the new Act, may prove to be a liability trap.

III. CONTROL

The old ULPA provides that a limited partner will lose his limited liability if he takes part "in the control of the business."³⁵ One of the most troublesome questions under the old Act is determining what constitutes an improper exercise of "control."³⁶

The revised Act generally carries over the prohibition against a limited partner's exercise of control, but makes two modifications. First, a limited partner who takes part in the control of the business is liable only to those who have actual knowledge of his participation, unless the exercise of control is "substantially the same as the exercise of the powers of a general partner."³⁷ According to the Comment to section 303, the uncertainties of the "control" test make it unfair to impose unlimited liability on a limited partner unless the third party has actual knowledge of the limited partner's control. Liability may still be imposed, however, if the limited partner exercises the same control as a general partner, but manages to prevent third parties from knowing of his control. While the

partnership name to conflict with that of any corporation on record, § 102(4), a centralized, integrated filing system will be required. While such a system requires a person seeking information about a limited partnership to check only a single source, rather than having to determine which county clerk's office to consult, and prevents confusion or possible deception resulting from the existence of an incorporated and an unincorporated business using the same name, the cost of such a system, especially in a populous state like New York, would be considerable, especially if present local filings are to be integrated in the unified list.

33. ULPA, Commissioners' Prefatory Note, (1976).

34. See H. Henn, *supra* note 2, § 29, at 67 n.2 (noting the dual philosophies of drafting limited partnership certificates under the old Act).

35. ULPA § 7 (1916).

36. J. Crane & A. Bromberg, *supra* note 2, § 26, at 147; see W. Cary, *Partnership Planning* 41 (1970); S. Rowley, *supra* note 1, § 53.7; Feld, *The "Control" Test for Limited Partnerships*, 82 Harv. L. Rev. 1471 (1969).

37. Section 303(a) of the revised Act provides: "Except as provided in subsection (d), a limited partner is not liable for the obligations of a limited partnership unless he is also a general partner or, in addition to the exercise of his rights and powers as a limited partner, he takes part in the control of the business. However, if the limited partner's participation in the control of the business is not substantially the same as the exercise of the powers of a general partner, he is liable only to persons who transact business with the limited partnership with actual knowledge of his participation in control."

actual knowledge provision is worthwhile, it seems inevitable that the section will transfer litigation from the uncertain determination of "control" to the almost equally vague determination of conduct "substantially the same as" that of a general partner.

Second, the new Act supplies "safe harbor" provisions enumerating activities which would not of themselves subject the limited partner to unlimited liability.³⁸ These provisions are based largely on the Delaware,³⁹ Nevada,⁴⁰ and Washington⁴¹ modifications of the old Act. Section 303(b) provides:

A limited partner does not participate in the control of the business . . . solely by doing one or more of the following:

- (1) being a contractor for or an agent or employee of the limited partnership or of a general partner;
- (2) consulting with and advising a general partner with respect to the business of the limited partnership;
- (3) acting as surety for the limited partnership;
- (4) approving or disapproving an amendment to the partnership agreement; or
- (5) voting on one or more of the following matters:
 - (i) the dissolution and winding up of the limited partnership;
 - (ii) the sale, exchange, lease, mortgage, pledge, or other transfer of all or substantially all of the assets of the limited partnership other than in the ordinary course of its business;
 - (iii) the incurrence of indebtedness by the limited partnership other than in the ordinary course of its business;
 - (iv) a change in the nature of the business; or
 - (v) the removal of a general partner.⁴²

The list of "safe" activities, specifically stated to be nonexclusive,⁴³ is an eminently desirable provision. Although the section as a whole clearly represents an improvement over the existing uniform Act, it does not appear to go far enough. For example, the effect of section 303(b)(2) on a leading case, *Plasteel Products Corp. v. Helman*,⁴⁴ is not clear. In that case, the limited partnership agreement provided that the general partner could exercise various financial powers only when he acted jointly with the limited partners' nominee, who was also designated as general sales

38. § 303(b).

39. Del. Code Ann. tit. 6, § 1707 (1974).

40. Nev. Rev. Stat. § 88.080 (1973).

41. Wash. Rev. Code Ann. § 25.08.070 (Supp. 1978). New York also specifies certain acts which will not constitute "control." N.Y. Partnership Law §§ 96, 99, 115-a (McKinney Supp. 1978).

42. § 303(b). It would also have been worthwhile for the section to have stated that the commencement of a derivative action, provided for by article 10 of the new Act, would not constitute an exercise of control. See pt. IX *infra*.

43. "The enumeration in subsection (b) does not mean that the possession or exercise of any other powers by a limited partner constitutes participation by him in the business of the limited partnership." § 303(c).

44. 271 F.2d 354 (1st Cir. 1959).

manager.⁴⁵ The agreement also required repurchase of the limited partners' interests if the nominee were discharged.⁴⁶ The court held that there was not a sufficient exercise of control by the limited partners to subject them to individual liability because, despite the repurchase provisions, the nominee could be discharged at any time.⁴⁷ The conduct in *Plasteel*, however, might well be construed as greater control than the standard of "consulting with and advising a general partner with respect to the business of the limited partnership,"⁴⁸ and might, therefore, expose the limited partners to personal liability. The statute ought to make clear whether the case is to be followed or overruled.

A similar uncertainty exists in relation to another leading case, *Holzman v. DeEscamilla*.⁴⁹ Contrary to the result in *Plasteel*, the limited partners were held to have participated in the control of a business in which "there was never any crop that was planted or contemplated in planting that wasn't thoroughly discussed and agreed upon" by the two limited partners and the general partner.⁵⁰ The general partner was, according to the court, "overruled" as to two crops; moreover, checks required the signatures of any two of the three partners, effectively vesting control of the partnership funds in the limited partners.⁵¹ Again, it is not clear under the statute whether such control would go beyond the scope of permitted activities, making the limited partners liable to those with, and possibly even to those without,⁵² knowledge of the exercise of such powers. At least a reference to the case in the Comment would have helped to clear up the matter.⁵³

There is also a policy question to consider. If there is no deception whereby an innocent third party is led mistakenly to believe that a limited partner is a general one, on whose personal liability the third party may depend, is it necessary to subject the limited partner to personal liability at all, irrespective of the amount of control he is

45. *Id.* at 355.

46. *Id.*

47. *Id.* at 356.

48. § 303(b)(2).

49. 86 Cal. App. 2d 858, 195 P.2d 833 (Dist. Ct. App. 1948).

50. *Id.* at 859, 195 P.2d at 834 (quoting record).

51. *Id.* at 860, 195 P.2d at 834.

52. § 303(a).

53. Another minor problem area that should probably have been dealt with explicitly by the new Act is whether personal liability would be imposed upon limited partners who exercise "control" of the limited partnership as officers, directors, or shareholders of a corporate general partner. *See* *Western Camps, Inc. v. Riverway Ranch Enterprises*, 70 Cal. App. 3d 714, 138 Cal. Rptr. 918 (Ct. App. 1977) (limited partners held not to incur personal liability by acting as officers, directors, or shareholders of corporate general partner); *Frigidaire Sales Corp. v. Union Properties, Inc.*, 88 Wash. 2d 400, 562 P.2d 244 (1977) (same). *But see* *Delaney v. Fidelity Lease Ltd.*, 526 S.W.2d 543 (Tex. 1975) (contra).

permitted to exercise by the general partners? Except to follow history, there seems to be no good reason why a limited partner should not be allowed to participate in management to the extent the general partners are willing to allow him to do so, provided they are willing to subject themselves to liability for his acts. A partnership, or even an individual, can appoint an agent to do any legal act, provided the appointing party is willing to assume the consequences. When an agent acts within the scope of the powers given him, he is not personally liable in contract to the outside party. It would seem logical to afford similar treatment to a limited partner, provided, just as in an ordinary agency, the third party is not misled.⁵⁴ When limited partners participate in control, the certificate filing provision required by the new Act would adequately inform a third party of the distinction between the liability of the general and limited partners. The internal relationship among limited and general partners should be the concern only of the latter. Accordingly, all personal liability of a limited partner should be eliminated unless he meets the tests for liability of a general partner or a partner by estoppel under the Uniform Partnership Act.⁵⁵

If tradition is to be maintained, however, the Delaware statute, which is the most liberal of the deviations from the current Act, is preferable to section 303. Most notably, the Delaware law provides that a limited partner's approval or disapproval of "such material matters related to the business of the partnership as shall be stated in the certificate and in the partnership agreement" shall not be deemed "control" for the purpose of establishing a limited partner's liability.⁵⁶ The Delaware provision, omitted in the new ULPA, would seem to protect the limited partners in both the *Plasteel* and *Holzman* decisions, provided the partnership purpose was clearly delineated in the partnership certificate and agreement.

IV. FINANCIAL MATTERS

A. Contributions

The new Act, reversing the old Act,⁵⁷ expressly allows not only cash and property, but also services rendered, and an obligation to perform

54. Section 303(d) is designed to prevent the flagrant misleading of creditors. "A limited partner who knowingly permits his name to be used in the name of the limited partnership, except under circumstances permitted by Section 102(2)(i), is liable to creditors who extend credit to the limited partnership without actual knowledge that the limited partner is not a general partner." § 303(d).

55. Uniform Partnership Act § 16.

56. Del. Code Ann. tit. 6, § 1707 (1974). It would also have been beneficial if the new Act had added to § 303(b)(5) the provision, contained in the Delaware statute, that voting on the election of general partners, as well as on their removal, is not an exercise of control.

57. ULPA § 4 (1916).

services, to constitute a partner's contribution.⁵⁸ The new Act also explicitly validates a contribution by way of "a promissory note or other obligation to contribute cash or property,"⁵⁹ which is permitted only by implication under the old Act.⁶⁰

The wisdom of these provisions is debatable. Allowing the future delivery of cash⁶¹ or property to constitute a present contribution does not seem dangerous to creditors⁶² because a limited partnership, unlike a corporation, offers creditors the added security of the general partners' personal liability.⁶³ Permitting contributions in the form of services to be rendered, however, seems certain to create problems. Section 502(a) of the new ULPA stipulates the procedure for enforcement of a partner's contribution:

Except as provided in the certificate of limited partnership, a partner is obligated to the limited partnership to perform any promise to contribute cash or property or to perform services, even if he is unable to perform because of death, disability or any other reason. If a partner does not make the required contribution of property or services, he is obligated at the option of the limited partnership to contribute cash equal to that portion of the value (as stated in the certificate of limited partnership) of the stated contribution that has not been made.⁶⁴

Subsection (b) goes on to provide that a partner's obligation to make a contribution may be compromised only by the consent of all partners, unless the partnership agreement provides otherwise. A creditor who has relied on the original obligation, however, may enforce it notwithstanding the compromise. The partnership cannot force the limited partner to perform the promised services; it can only compel him to contribute in cash the difference between the value of any partial performance and the agreed value of the services as stated in the certificate. If a partner has performed only in part, and that partial performance is overvalued, allowing a relatively small cash contribu-

58. § 501. The drafters of the new Act may have been influenced by the argument that future services should be allowed as consideration for the issuance of shares in a corporation. See Herwitz, *Allocation of Stock Between Services and Capital in the Organization of a Close Corporation*, 75 Harv. L. Rev. 1098 (1962).

59. § 501.

60. See ULPA § 17(1)(b) (1916) (a limited partner is liable for "any unpaid contribution which he agreed in the certificate to make in the future").

61. Future payment of cash is frequently prohibited as consideration for the issuance of corporate shares. See, e.g., N.Y. Bus. Corp. Law § 504(b) (McKinney 1963); ABA-ALI Model Bus. Corp. Act § 19 (1971).

62. But see Gregory, *The Financial Provisions of the Revised Uniform Limited Partnership Act: Articles 5 and 6*, 9 St. Mary's L.J. 479, 481 (1978), which states that "section 501 could be greatly improved from the standpoint of clarity in drafting, for it leaves open the possibility that an obligation to contribute property twenty years in the future is a permissible form of contribution by a limited partner."

63. Of course, a corporation may be a general partner in most states. See note 9 *supra* and accompanying text.

64. § 502(a).

tion to make up the remainder of the agreed value could permit the actual value of the contribution to be less than stated without liability. Prejudice to creditors,⁶⁵ as well as to present and future partners, would result.⁶⁶

B. *Profits, Losses, and Distributions*

Sections 503 and 504 of the new Act provide "default law" rules—rules to take effect in the absence of contrary agreement—to govern the sharing of profits and losses, and distributions, among both the general and limited partners. The profits and losses are to be "allocated on the basis of the value (as stated in the certificate of limited partnership) of the contributions made by each partner to the extent they have been received by the partnership and have not been returned."⁶⁷ Distributions are to be made on the same basis.⁶⁸

The Comments to these sections state that the old Act did not provide a default law basis for the sharing of profits and losses and distributions. This statement is not completely accurate, in that the old Act requires that the certificate "shall state . . . [t]he share of the profits or other compensation by way of income which each limited partner shall receive by reason of his contribution,"⁶⁹ and contains a similar provision as to returns of contribution.⁷⁰ The new Act provides that the limited partnership certificate shall set forth any right of a partner to receive distributions of property, including cash,⁷¹ and any right of a partner to receive a distribution which includes a return of any part of his contribution.⁷² The right of a partner to receive a distribution upon the termination of his membership in the limited partnership, however, need be included only if agreed upon.⁷³ Apparently, the new Act does not make a certificate provision on the subject of distributions mandatory unless the distributions include a return of contribution

65. For example, the same problems noted by Professor Herwitz in connection with watered stock and corporate dissolution, *see* Herwitz, *supra* note 58, at 1105-06, would seem equally applicable to a partnership if future services are to be permitted as contributions.

66. Section 502 contains further drafting deficiencies. It is unclear, for example, whether the obligation to contribute in the future could be enforced by a new limited or general partner, or an assignee, if the partnership itself did not elect to compel a contribution in cash.

67. § 503. This section states in full: "The profits and losses of a limited partnership shall be allocated among the partners, and among classes of partners, in the manner provided in the partnership agreement. If the partnership agreement does not so provide, profits and losses shall be allocated on the basis of the value (as stated in the certificate of limited partnership) of the contributions made by each partner to the extent they have been received by the partnership and have not been returned." Section 504 of the new Act is identical with respect to distributions.

68. § 504.

69. ULPA § 2(1)(a)(ix) (1916).

70. *Id.* § 2(1)(a)(xiv).

71. § 201(a)(9).

72. §§ 201(a)(10), 601(2).

73. § 201(a)(8).

prior to withdrawal.⁷⁴ This lack of a clear distinction between permissive and mandatory provisions is a drafting deficiency of the new Act.

The Comments to the new Act are correct, however, in the sense that the old Act does not make express provisions for distribution rights as to general partners.⁷⁵ It does, however, grant the general partners the same rights as partners in an ordinary partnership,⁷⁶ thereby incorporating the provisions of the Uniform Partnership Act (UPA).⁷⁷ Unfortunately, the new ULPA provides "default" rules as to distribution which are at variance with those in the UPA.⁷⁸ Moreover, from a drafting standpoint, the references in the new ULPA to "contributions made by each partner *to the extent they have been received*"⁷⁹ seems destined to cause interpretive problems in view of the allowance of future services as contributions.

In addition, article 6 of the new Act states that both limited and general partners may obtain "interim distributions"—distributions made prior to a partner's withdrawal—at the time and to the extent specified in the partnership agreement.⁸⁰ If, however, the distribution includes a return of the partner's contribution, the limited partnership certificate must specify when and how the distribution may be made.⁸¹

The relationship between this section and the "default law" rules is not clear. Although section 601 seems to require an agreement, even if there is no agreement as to distribution a partner would presumably be entitled to a distribution determined, in the absence of agreement, by section 504. Clarification and cross-reference between sections 601 and 504 appears necessary, especially since section 606 grants creditor status to a partner who is entitled to a distribution,⁸² conferring on partners a status equal to the outside creditors.

74. Although § 201(a)(9) could be construed as a blanket provision, requiring that all rights to receive distributions from the limited partnership be stated in the certificate, such a reading seems to conflict with § 604. Section 604 states: "Except as provided in this Article, upon withdrawal any withdrawing partner is entitled to receive any distribution to which he is entitled under the partnership agreement and, if not otherwise provided in the agreement, he is entitled to receive, within a reasonable time after withdrawal, the fair value of his interest in the limited partnership as of the date of withdrawal based upon his right to share in distributions from the limited partnership." (emphasis added). The reference to the partnership agreement in § 604 would imply that the certificate provisions as to distributions are permissive, not mandatory.

75. See ULPA § 9 (1916).

76. *Id.*

77. Uniform Partnership Act § 18(a).

78. The Uniform Partnership Act § 18(a) provides that all partners should be repaid their contributions, and then share equally in the remaining profits or surplus. The new ULPA states that distributions should be made on the basis of the contributions received by the partnership and not yet returned. § 504.

79. §§ 503, 504 (emphasis added).

80. § 601(1).

81. § 601(2).

82. See notes 86-88 *infra* and accompanying text.

Section 605 carries over in part the provisions of the prior law by providing that a partner has no right to receive any distribution except in cash, regardless of the nature of his contribution.⁸³ Unlike the old law, however, the new Act apparently requires a certificate provision to authorize a non-cash distribution.⁸⁴ According to the Comment to section 605, the section is designed to "protect a limited partner (and the remaining partners) against a distribution in kind of more than his share of particular assets."⁸⁵ It is unclear why such protection is necessary, but, presumably, it is designed to avoid an unfair shifting of tax benefits and liabilities. Nevertheless, it is unclear how much protection will actually be afforded other partners by a provision that the withdrawing partner cannot be compelled to accept more than his share.

Section 606 confers creditor status upon a partner once he "becomes entitled to receive a distribution."⁸⁶ This provision dangerously dilutes outside creditor protection because it applies even to general partners. Fortunately, section 607 provides that a partner may not receive a distribution if it would render the partnership insolvent. Further, section 608 obligates all partners to repay rightful and wrongful returns of their contributions when necessary to meet liabilities to creditors, but, unlike the old Act,⁸⁷ imposes a time limit on the obligation.⁸⁸ While requiring a partner to repay such returns is a wise creditor safeguard, it does seem inconsistent with section 606, which characterizes partners as "creditors" as to distributions.

C. *Withdrawal*

Upon withdrawal, a partner, unless otherwise provided in the partnership agreement, is entitled to "the fair value of his interest in the limited partnership as of the date of withdrawal based upon his right to share in distributions from the limited partnership."⁸⁹ Read together with the applicable default law rules, this would mean that,

83. Compare § 605 with ULPA § 16(3) (1916).

84. ULPA § 16(3) (1916) states that the consent of all the partners is sufficient to permit non-cash distributions.

85. § 605, Comment.

86. "At the time a partner becomes entitled to receive a distribution, he has the status of, and is entitled to all remedies available to, a creditor of the limited partnership with respect to the distribution." § 606.

87. ULPA § 17(2)(b) (1916).

88. The section imposes a six-year period of limitation, during which the partner is liable to return any distribution containing a part of his contribution. § 608.

89. § 604. Apparently, "interest in the limited partnership" as it is used in § 604 does not mean the same as "partnership interest," which is defined in § 101(10) to mean "a partner's share of the profits and losses of a limited partnership and the right to receive distributions of partnership assets." If the two terms were equated, the circularity of the definitions would be obvious. "Interest in the limited partnership" seems to mean something closer to "book value."

absent a provision in the agreement, a withdrawing partner would be entitled to a distribution upon withdrawal determined by multiplying the percentage of his total contribution, as received by the partnership and not yet returned,⁹⁰ by the value of the partnership assets at the time of withdrawal. The complexity of the default law provisions gives an added incentive to limited partnership organizers to draft a detailed partnership agreement.

D. *Priorities*

Section 804 provides new priority rules to govern the winding up of a limited partnership. The Comment to the section summarizes them:

Section 804 revises Section 23 of the prior uniform law by providing that (1) to the extent partners are also creditors, other than in respect of their interests in the partnership, they share with other creditors, (2) once the partnership's obligation to make a distribution accrues, it must be paid before any other distributions of an "equity" nature are made, and (3) general and limited partners rank on the same level except as otherwise provided in the partnership agreement.⁹¹

The wisdom of the policy decisions implicit in the Comment is extremely dubious. If the goal of the new ULPA is to equalize the treatment of limited partnerships with that of corporations, then, by analogy, limited partners resemble preferred shareholders vis-a-vis the "common" shareholders, the general partners. Accordingly, limited partners should have a priority in winding up to the extent of their limited interest. Even more questionable is the rule giving any partner, general or limited, a status equal to outside creditors with respect to loans to the business. Old ULPA section 13, providing that limited partners share claims for money lent to the partnership *pro rata* with general creditors, and section 23, giving non-partner creditors priority over partner creditors as to partnership assets, seem to provide a fairer order of repayment.

Furthermore, new section 804 raises the question, frequently litigated in the corporate context, of whether loans are genuine, or merely disguised contributions to capital. If all insider "loans" are upheld, merely because they are characterized as loans, the Act will give a distinct advantage to the limited partnership over its corporate analogue, but only until creditors realize the insecurity of their position.

90. Once again, the acceptance of future services as a contribution would appear to create difficulties in calculating shares.

91. § 804, Comment. Under the old law, creditors were paid first, followed by payments to limited partners both as to profits and returns of contribution, with general partners having least priority. ULPA § 23 (1916). The apparent effect of § 804 is to "bracket" limited and general partners together. Even though this order of repayment can be varied by the partnership agreement, the section significantly downgrades the rights of limited partners.

Apparently, recognition of all loans by a partner to the partnership was not intended. The Comment to section 107, expressly authorizing loans by both general and limited partners, addresses the problem: "Of course, other doctrines developed under bankruptcy and insolvency laws may require the subordination of loans by partners under appropriate circumstances."⁹² The Comment, however, provides no real solution, since what law exists on the subject in the corporate field is far from consistent.⁹³

The new Act also omits the prohibitions of old ULPA section 13 against repayment of loans made by limited partners when the partnership does not have sufficient assets to discharge partnership liabilities to non-partners, and against limited partners receiving or holding partnership property as collateral security for their loans. The second prohibition has been interpreted so as to allow a limited partner to become a secured creditor when the partnership was not insolvent when the security was given⁹⁴—an interpretation which was hardly mandated by the language of the provision. Nevertheless, under the new Act these matters are to be left to be resolved by the enacting state's fraudulent conveyance statute. The omission is probably justified because the Uniform Fraudulent Conveyance Act, section 8, probably gives sufficient protection to creditors in both instances covered by section 13.

The new Act apparently allows both general and limited partners to make secured loans, provided they are made while the partnership meets the solvency requirements of the Fraudulent Conveyance Act.⁹⁵ If the wisdom of allowing ordinary loans by general partners is dubious, however, allowing secured loans is doubly so, since general partners will then enjoy priority over all other partners. At best, this will mean priority of the general partner's personal creditors over his business creditors. Despite a superficial appearance of modernity, therefore, it is by no means clear that the financial provisions of the new Act represent an improvement in policy or clarity over the old ULPA.

V. TRANSFERS

One of the attractive features of the limited partnership form for small businesses is the principle of *delectus personarum*: partnership interests, including those in a limited partnership, are not freely transferable. Although a share in the profits is assignable, substitution

92. § 107, Comment.

93. See *Costello v. Fazio*, 256 F.2d 903 (9th Cir. 1958), H. Henn, *supra* note 2, § 152.

94. *Hughes v. Dash*, 309 F.2d 1 (5th Cir. 1962). See generally J. Crane & A. Bromberg, *supra* note 2, § 93, at 550.

95. Uniform Fraudulent Conveyance Act § 8.

of the transferee in the business requires consent of the remaining partners unless the agreement provides otherwise.⁹⁶

As Professor O'Neal has indicated with respect to close corporations, "shareholders . . . usually desire to retain the power to choose future associates."⁹⁷ The reasons for this desire are common to the partnership as well as to the small corporation; for example:

Each shareholder wants to be in a position to prevent outsiders from entering the business if he doubts their integrity or business judgment, or feels that working with them would be unpleasant or unrewarding. . . . A purchaser of shares may have neither the ability nor the desire to do the work previously performed by his vendor, or he may not be able to work congenially with the other participants.⁹⁸

Although some recent corporate statutes have recognized the importance of transfer restrictions to close corporations,⁹⁹ there is still some doubt as to the validity of transfer restrictions in many states,¹⁰⁰ especially as to those restrictions which require the consent of the remaining participants.¹⁰¹ Therefore, the absolute availability of such restrictions in the partnership is still one of its principal advantages over the corporation for small businessmen.

While a limited partner's interest is ordinarily assignable,¹⁰² the new Act carries over the old law's implied requirement that the admission of a new general or limited partner to membership requires the consent of all partners. In a clarification of the requirements of the prior law, the new ULPA provides that, after the original filing, the admission of new general partners requires the specific written consent of each partner.¹⁰³ If the interest is acquired directly from the partnership, additional limited partners may be admitted pursuant to the partnership agreement or, if the agreement is silent, upon written consent of all partners.¹⁰⁴ An assignee of a limited partnership interest may also become a limited partner if his assignor, pursuant to a certificate provision, has the right to confer such status upon him, or if all the partners consent.¹⁰⁵ In the case of the additional partner, the individ-

96. ULPA § 19 (1916).

97. 2 F. O'Neal, *Close Corporations* § 7.02 (1971).

98. *Id.*

99. *Id.* § 7.06 a.

100. *Id.* §§ 7.06, .09, .10.

101. *Id.* § 7.08.

102. Section 702 follows ULPA § 19(1) (1916) in making a limited partner's interest generally assignable.

103. § 401. The old Act required the consent of all *limited* partners to the addition of a new general partner, ULPA § 9(1)(e) (1916), but did not expressly require consent of all general partners as well. *But see* ULPA § 25(1)(b) (1916) (requiring all members of the partnership to sign any amendment to the certificate adding a limited or general partner). Section 704(a) allows an assignee of a general partner to become a limited partner only. The new Act might have achieved greater clarity by completely separate treatment of general and limited partners, rather than using "partner," except where qualified, to refer to both. § 101(8).

104. § 301.

105. § 704.

ual will become a limited partner only upon amendment of the limited partnership certificate.¹⁰⁶

Although there is nothing objectionable about allowing the partnership to restrict the assignment of limited partnership interests,¹⁰⁷ there is uncertainty created by the Comment to the assignment section as to the exact extent to which such restrictions are valid. The Comment states that "there was no intention to affect in any way the usual rules regarding restraints on alienation of personal property."¹⁰⁸ Moreover, the restriction requiring "specific written consent" of each partner, limited and general, to the admission of any new general partner is unwise, especially since the Comment states that such consent "must specifically identify the general partner involved."¹⁰⁹ This requirement seems to preclude any advance authorization for the admission of new general partners, and seems overly restrictive. The Uniform Partnership Act, in contrast, has no such requirement for written consent.¹¹⁰

From a policy standpoint, it might have been simpler to reverse the direction of the statute by making limited partnership interests freely transferable subject to restriction by the agreement.¹¹¹ Because the status of limited partners is, as has been suggested, analogous to that of preferred shareholders, and their intrusion into the operation of the business is even more circumscribed, free transferability of the limited partners' interests, once their full agreed contribution has been made, is probably more often desired than not. In any event, an express authorization for fractionalization of interest, without the necessity for certificate amendment,¹¹² would have been desirable, especially in large investment partnerships.

The new Act's treatment of assignees who become limited partners is analogous to the treatment of a bona fide transferee of watered stock. Thus, an assignor limited partner remains liable for his contribution

106. § 301(b). The condition of certificate amendment might be inferred as to assignees as well. See note 21 *supra*. The new Act also makes certain stylistic changes, eliminating the term "substituted" limited partner found in ULPA § 19(2) (1916). § 704. It also states that a partner's interest is assignable "in whole or in part." § 702.

107. See *Chaiken v. Employment Security Comm'n*, 274 A.2d 707, 709 (Del. Super. Ct. 1971).

108. § 702, Comment.

109. § 401, Comment.

110. See Uniform Partnership Act § 18(g).

111. Of course, the partnership certificate can always make free transferability the rule. § 704. Moreover, free transferability has its own dangers. Free transferability of interest is a factor which points to corporate taxation. Treas. Reg. § 301.7701-2(e) (1960). Free transferability, however, was not fatal to the taxation of a limited partnership as a partnership in *Larson v. Commissioner*, 66 T.C. 159 (1976). Retention of the old rule might have been dictated by a desire on the part of the drafters to avoid possible taxation of a limited partnership formed under the new Act as a corporation. See Haims & Strock, *supra* note 8, at 517-18, 521.

112. §§ 202(b), 702.

and any false statements made in the certificate.¹¹³ The assignee is, however, at least liable for his assignor's other obligations, except for those which were unknown to the assignee and which he could not discover from the certificate.¹¹⁴ Once again, the effect which the new Act's liberality regarding future services will have on the assignee's ability to fulfill the assignor's obligations is unclear.

Additionally, section 705 of the revised Act states that the estate of a partner may, for settlement and administration purposes, exercise all the late partner's rights, including the right to confer limited partner status on an assignee. But the estate's liabilities, as opposed to rights, are not prescribed. The Comment states that in drafting the section, "[f]ormer [ULPA] Section 21(2), making a deceased limited partner's estate liable for his liabilities as a limited partner was deleted as superfluous, with no intention of changing the liability of the estate."¹¹⁵ Yet the liability of a partner's estate where the business is continued is one of the most troublesome areas of partnership law.¹¹⁶ A more explicit treatment, rather than avoidance of the problem, would have been welcome.

A related matter is the right of the limited partners to information about the business. Old ULPA section 10 gives the limited partners the right to inspect and copy the partnership books, and to receive a "formal account of partnership affairs, whenever circumstances render it just and reasonable."¹¹⁷ The right to information under the new Act is established by reading two sections together. Section 105 recites the records to be kept by a limited partnership, but makes no specific reference to the books of account. Section 305 mandates that limited partners have access to the specified records and "other information regarding the affairs of the limited partnership as is just and reasonable."¹¹⁸ Even preferred shareholders generally have greater inspection rights.¹¹⁹ Since limited partners are "locked in," unlike preferred shareholders who can generally transfer their shares, it would seem fairer to give them broader inspection rights than those afforded by the vague "just and reasonable" standard.

113. § 704(c).

114. § 704(b). Non-release of the assignor does not preclude assignee liability for the same obligation.

115. § 705, Comment.

116. W. Cary, *supra* note 36, at 55. Section 702 states that "[e]xcept as provided in the partnership agreement, a partner ceases to be a partner upon assignment of all his partnership interest." The effect on a general partner's liabilities is not spelled out. Section 403 merely cross-references to the liabilities of a general partner in an ordinary partnership.

117. ULPA § 10(b) (1916).

118. § 305(2)(iii).

119. See N.Y. Bus. Corp. Law § 624 (McKinney 1963); ABA-ALI Model Bus. Corp. Act § 52 (1971); 2 F. O'Neal, *supra* note 97, § 7.03. Despite the elaborate list of records to be kept, § 105, in which the limited partner has an inspection right, § 305, the actual books of account are omitted. The word "any" before "financial statements" in § 105 obviously does not mandate their preparation, and access to "full information regarding the state of the business and financial condition" in § 305 is ambiguous as to any right to examine the actual records of account.

VI. WITHDRAWAL

Sections 402 and 602 provide the rules governing the withdrawal of a general partner, while section 603 contains the corresponding provisions for a limited partner. Other than the provision in section 602, which entitles the limited partnership to recover damages from a general partner who withdraws in violation of the partnership agreement,¹²⁰ but which is unclear as to whether the damages may exceed the general partner's share of distributions,¹²¹ the principal importance of the withdrawal sections is in relation to the dissolution of the partnership. The new Act conceptually distinguishes between withdrawal,¹²² on the one hand, and dissolution,¹²³ winding up,¹²⁴ and continuation¹²⁵ on the other. This categorization differs from that of the Uniform Partnership Act, which distinguishes between events causing dissolution, and winding up.¹²⁶ In the UPA, dissolution and termination, which follows upon winding up, are not synonymous.¹²⁷ In contrast, the new Limited Partnership Act generally equates dissolution and termination unless the conditions for continuation of the entity are met.¹²⁸ Therefore, the new Act's incorporation of the Uniform Partnership Act¹²⁹ may pose interpretive problems because of the inexact congruence. A redrafting of both Acts concurrently might have avoided this difficulty by enabling an exact cross-reference to the UPA for all provisions pertaining to general partners. At any rate, the terminology of the new Act is ambiguous. Ideally, an "event of withdrawal" should give a right to "winding up," absent a provision for "continuation." The additional references to dissolution and termination, as well, in the new Act, only confuse matters.

VII. DISSOLUTION

The old Act contained rather scant provisions on dissolution¹³⁰ and none on winding up except for the provision that a limited partner had the

120. No such liability attaches for the withdrawal of a limited partner.

121. § 602: *See* Uniform Partnership Act § 38(2)(II) (stating merely that the partners have a right to damages for breach of the agreement).

122. §§ 402, 602, 603. *See also* § 101(3) (" 'Event of withdrawal of a general partner' means an event that causes a person to cease to be a general partner as provided in Section 402. ").

123. §§ 801, 802. Under § 801, dissolution is to be followed by winding up unless there is continuation under § 801(3). *See also* § 303(b)(5)(i) (allowing voting on the dissolution and winding up of a limited partnership).

124. § 803.

125. § 801(3).

126. *See* Uniform Partnership Act § 30 ("On dissolution the partnership is not terminated, but continues until the winding up of partnership affairs is completed. ").

127. *See* Uniform Partnership Act §§ 29, 30; J. Crane & A. Bromberg, *supra* note 2, § 73.

128. § 801(3). Section 201(a)(8) allows the limited partnership certificate to fix the terms and conditions of termination and distribution.

129. § 1105.

130. ULPA §§ 9(1)(g), 16, 20 (1916).

right to dissolve the partnership and have its affairs wound up if the partnership was unable or unwilling to make repayment of the limited partner's contribution.¹³¹ The revised Act substitutes an entire detailed article on dissolution.¹³² Generally, withdrawal and dissolution under the new Act have the same results as under the old law. Thus, the death or withdrawal of a limited partner does not affect the continued existence of the partnership.¹³³ The death, withdrawal, or insanity of a general partner continues to result in the dissolution of the partnership¹³⁴ subject to section 801, which allows for continuation of the partnership if another general partner is available or if a replacement can be agreed upon.¹³⁴ When such continuation is not possible, winding up will follow dissolution.¹³⁵

The events that constitute withdrawal of a general partner, and therefore lead to dissolution, have been precisely defined by the new Act.¹³⁶ Withdrawal may include the voluntary withdrawal of a general partner, even if in violation of the partnership agreement;¹³⁷ the assignment of a partner's entire interest;¹³⁸ or the removal of a partner pursuant to the agreement.¹³⁹ Another event of withdrawal has been added to take account of corporations that become general partners: corporate dissolution is now the equivalent of death as to a corporate partner.¹⁴⁰ The

131. ULPA § 16(4) (1916).

132. Art. 8.

133. Compare §§ 603, 705 of the new Act with ULPA §§ 16, 21 (1916).

134. §§ 402, 801(3).

135. "A limited partnership is dissolved and its affairs shall be wound up upon the happening of the first to occur of the following:

(1) at the time or upon the happening of events specified in the certificate of limited partnership;
(2) written consent of all partners;

(3) an event of withdrawal of a general partner unless at the time there is at least one other general partner and the certificate of limited partnership permits the business of the limited partnership to be carried on by the remaining general partner and that partner does so, but the limited partnership is not dissolved and is not required to be wound up by reason of any event of withdrawal if, within 90 days after the withdrawal, all partners agree in writing to continue the business of the limited partnership and to the appointment of one or more additional general partners if necessary or desired; or

(4) entry of a decree of judicial dissolution under Section 802." § 801.

136. § 402. The introductory paragraph of the section, however, contains an instance of poor draftsmanship. It would appear that a partner who has withdrawn because of death or insanity would nevertheless be required to give his consent to the continuation of the partnership. The language should be changed to clarify the matter: "Except as approved by the specific written consent of all [remaining] partners at the time, a person ceases to be a general partner of a limited partnership upon the happening of any of the following events: . . ." § 402.

137. §§ 402(1), 602.

138. §§ 402(2), 702.

139. § 402(3).

140. § 402(9). The dissolution and winding up of a general partner which is a separate partnership has the same effect as a corporate partner's dissolution, as does the distribution of an estate which holds a partnership interest. § 402(8), (10).

bankruptcy of a general partner will also constitute withdrawal,¹⁴¹ as will other bankruptcy related events.¹⁴² In addition, insanity has been defined to mean an adjudication of incompetence, correcting an anomaly in the old Act.¹⁴³

The dissolution article is not without problems, however. Section 801(3) provides for a ninety-day period after an event of withdrawal during which all partners may agree in writing to the continuation of the business.¹⁴⁴ The effect of this section is to create an extended limbo period during which it is uncertain whether the partnership will continue. Moreover, the winding up provisions of section 803 fail to make reference to this ninety-day time span, creating uncertainty as to the effect which it will have on winding up.¹⁴⁵ Neither is it clear whether the general partners' agency powers to bind the partnership will continue through the ninety days, despite the new Act's incorporation of the Uniform Partnership Act's provisions on that subject.¹⁴⁶

VIII. FOREIGN LIMITED PARTNERSHIPS

In an attempt to remedy a problem area under the old law,¹⁴⁷ article 9 of the new Act provides detailed rules on the right of a limited partnership to do business in a state other than that of its formation. The provisions of the new Act regarding these foreign limited partnerships parallel those of statutes dealing with the qualification of foreign corporations to do business within another state.

Procedurally, the new Act requires that foreign limited partnerships apply for a certificate of registration from any state in which they seek to

141. § 402(4). The old Act was silent on the subject of bankruptcy, although under the Uniform Partnership Act § 31(5) the bankruptcy of a partner brought about dissolution.

142. § 402(4), (5). Subsection (5) appears to be defective in permitting the mere bringing of an action for dissolution of a corporate partner, rather than a judgment of dissolution, to cause the partnership to be dissolved. An action for corporate dissolution is so unlikely to succeed that it should not be made a sufficient condition for the dissolution of a limited partnership.

143. § 402(6)(ii). While the Uniform Partnership Act § 32(1)(a), (b) set out an "incompetence" standard, similar to the new Act, ULPA § 20 (1916) uses the word "insanity" only, without reference to any adjudication.

145. Winding up may be accomplished by general partners who have not wrongfully dissolved the partnership or, if no such general partners exist, by the limited partners. A court may also wind up a partnership upon the application of a partner, his legal representative, or his assignee. § 803. The standard for judicial dissolution, however, is troublesome. Section 802 allows judicial dissolution "whenever it is not reasonably practicable to carry on the business in conformity with the partnership agreement." This test seems unnecessarily vague when contrasted to the detail provided by Uniform Partnership Act § 32.

146. The old Act was silent as to the effect of dissolution on the agency powers of the general partners. Although the new Act states in § 1105 that the Uniform Partnership Act will govern any cases not provided for, the relevant provision, Uniform Partnership Act § 9, is not readily applicable to such a ninety-day limbo period.

147. J. Crane & A. Bromberg, *supra* note 2, § 22A, at 108-09.

do business.¹⁴⁸ The application for registration need only set forth basic information concerning the partnership, including the general character of the business, the agent for service of process, and the names and addresses of partners.¹⁴⁹ While the registration must be amended upon any change in the information,¹⁵⁰ presumably to protect creditors, it need not set out the amount of the partners' contributions—a more crucial creditor concern.¹⁵¹ Failure to register as a foreign limited partnership results in disqualification to sue in the foreign state,¹⁵² and a state official may seek to enjoin an unregistered partnership from doing business in the state of disqualification.¹⁵³

The introductory section of the new article combines two substantive rules governing foreign limited partnerships.

Section 901. [Law Governing.] Subject to the Constitution of this State, (1) the laws of the state under which a foreign limited partnership is organized govern its organization and internal affairs and the liability of its limited partners, and (2) a foreign limited partnership may not be denied registration by reason of any difference between those laws and the laws of this State.¹⁵⁴

This section appears to be influenced by the Model Business Corporation Act,¹⁵⁵ but differs in two material respects. First, under the new Act, a state may bar the admission of a foreign limited partnership or regulate its internal affairs only if authorized to do so by a state constitutional provision. Second, the new Act, unlike the Model Act, fails to limit the permissible activities of a foreign limited partnership to those businesses in which domestic limited partnerships may engage.

New York has recently proposed its own solution to the problem of foreign limited partnerships through an amendment to the Partnership Law.¹⁵⁶ In brief, the new New York statute requires a foreign limited partnership to have a certificate of authorization, issued by the department of state, before doing business or holding real property in the

148. § 902. The secretary of state will issue the certificate of registration upon payment of the necessary fees. § 903. The foreign limited partnership may even register under a name other than the one used in the state of its formation, provided the name contains the words "limited partnership."

149. § 902.

150. § 905. There is no provision for voluntary amendment of the registration, as is provided for a domestic partnership in § 202(d). Article 9 of the revised Act apparently does not require the registration to be cancelled even if the certificate of limited partnership in the state of organization is cancelled.

151. Compare § 902 with § 201(a)(4), (5). If the information as to contributions is important enough to warrant inclusion in the original certificate, its inclusion would seem equally important in foreign partnership filings. Filing with the foreign state a copy of the limited partnership certificate that is on file with the home state would seem to be a reasonable requirement—one which New York has recently adopted. See note 159 *infra* and accompanying text.

152. § 907.

153. § 908.

154. § 901.

155. See ABA-ALI Model Bus. Corp. Act § 106 (1971).

156. Act of July 10, 1979, ch. 519, 1979 N.Y. Laws 1073 (McKinney) (effective Jan. 1, 1980) (to be codified at N.Y. Partnership Law §§ 120 to 120-l (McKinney)).

state.¹⁵⁷ It also sets forth a non-exclusive list of activities which will not constitute "doing business."¹⁵⁸ The foreign limited partnership must file a copy of the certificate under which it is organized in its home state, and must provide additional information about partners, contributions, assignment, and priorities if it is not contained therein.¹⁵⁹ The partnership must also designate the secretary of state as its agent for the service of process, and must specify its principal place of business within New York.¹⁶⁰

The issuance of a certificate of authority permits the foreign limited partnership to do in New York any business "which may be done lawfully in [New York] by a limited partnership organized under the laws of [New York], to the extent that it is authorized to do such business in the state, territory, or country where it was created, but not other business."¹⁶¹ The "rights, powers and privileges" to be exercised by the partners of foreign limited partnerships are limited to those enjoyed by partners of domestic limited partnerships.¹⁶² The failure to register does not render the contracts of the foreign partnership invalid, but the partnership may not maintain any action or special proceeding within the state, although it may defend suits brought against it.¹⁶³ As under the new ULPA, the state attorney general may bring an action to restrain an unauthorized limited partnership from doing any business within New York.¹⁶⁴

This new article of the New York Partnership Law seems preferable to its counterpart in the revised ULPA. First, the New York provision prohibiting a foreign limited partnership from doing any business prohibited to a domestic limited partnership is probably a wise one, because it avoids any inequity in the treatment of local and foreign businesses. Moreover, a conflict between the Partnership Law and the various New York statutes prohibiting the conduct of certain businesses by limited partnerships or nonresidents is also avoided.¹⁶⁵ Second, because the New

157. *Id.* § 120-a(1).

158. *Id.* § 120-a(2).

159. *Id.* § 120-b(1), (2).

160. *Id.* § 120-b(2).

161. *Id.* § 120-b(3).

162. *Id.*

163. *Id.* § 120-f.

164. *Id.* § 120-h.

165. The New York Constitution does not contain any limitations upon the businesses which may be conducted by partnerships; therefore, § 901 of the new ULPA would not empower the state to place any restrictions on the internal affairs or admission of a foreign limited partnership. The new New York amendment, on the other hand, allows that state to give effect to various statutory restrictions on the partnership form. *See, e.g.*, N.Y. Pub. Health Law § 2801-a(4)(c) (McKinney 1977) (a hospital shall not be operated by a limited partnership); N.Y. Banking Law § 180 (McKinney 1971) (partnerships not qualifying as private bankers may not engage in banking); N.Y. Gen. Bus. Law §§ 455, 456 (McKinney 1968) (partnerships other than law firms may not engage in "budget planning"); N.Y. Real Prop. Law §§ 441, 441-b (McKinney 1968 & Supp. 1978) (special licensing requirements of partnerships of real estate brokers). As to admission requirements, there would seem to be no constitutional problem under either the new Act or the New York statute, since foreign

York amendment allows partners only the same "rights, powers and privileges" as partners in domestic limited partnerships, New York appears to exercise a degree of control over the internal affairs of the foreign limited partnership. Thus, if foreign limited partnerships are subject to the same rules of liability as New York limited partnerships, the potential "race" by limited partnership organizers to form the entity under the more liberal laws of another jurisdiction, as has occurred with corporations, would be eliminated.¹⁶⁶ Third, the New York statute exhibits a highly desirable and fairly complete degree of congruence with the New York corporation law. For example, the list of activities which will not constitute "doing business" is virtually identical to the list contained in the Business Corporation Law.¹⁶⁷ Accordingly, no confusion will exist as to whether activities conducted by one business form have the same consequences when conducted by the other.

IX DERIVATIVE ACTIONS

Article 10 of the new Act allows a limited partner to maintain a derivative action against the general partners for their misconduct. In doing so, the new Act follows the example of New York¹⁶⁸ and Delaware¹⁶⁹ amendments to the old Act, as well as prior decisional law.¹⁷⁰ Because the rights of limited partners are similar to those of corporate shareholders, the new Act's article on derivative actions has drawn on the corporate law. Section 1002 requires that the derivative plaintiff be a partner both at the time of the bringing of the action and at the time of the allegedly improper transaction, or have taken his interest directly from one who was a partner at such time—a requirement typical of corporation statutes.¹⁷¹ Section 1003, also relying on corporation law,¹⁷² requires that a demand on the general partner to bring the action, or a suitable excuse

partnerships appear to be subject to no more onerous requirements than local ones. See J. Crane & A. Bromberg, *supra* note 2, § 22A, at 108; H. Henn, *supra* note 2, § 98, at 161. Moreover, if a restriction on the admission of an out of state partnership were constitutionally invalid, it would be so regardless of whether it appeared in the state constitution or in a statute. Thus, the requirement of § 901 of the new Act, mandating that such restrictions be part of the state constitution, seems superfluous.

166. States have generally refrained from regulating the internal affairs of foreign corporations. W. Fletcher, *Cyclopedia of the Law of Private Corporations* § 8425 (rev. perm. ed. 1977). However, because of the ambivalent nature of the limited partnership—part entity, part aggregate—subjecting them to local law would not, presumably, be constitutionally infirm. Cf. *Hemphill v. Orloff*, 277 U.S. 537 (1928) (foreign business trust, having association and corporate characteristics, may be subjected to local state regulation).

167. Compare Act of July 10, 1979, ch. 519, § 120-a(2), 1979 N.Y. Laws 1073 (McKinney) (effective Jan. 1, 1980) (to be codified at N.Y. Partnership Law § 120-a(2) (McKinney)) with N.Y. Bus. Corp. Law § 1301(b) (McKinney 1963). The new enactment omits only that portion of § 1301(b) dealing with transactions in a corporation's own securities.

168. N.Y. Partnership Law §§ 115 to 115-c (McKinney Supp. 1978).

169. Del. Code Ann. tit. 6, § 1732 (1974).

170. E.g., *Lichtyger v. Franchard Corp.*, 18 N.Y.2d 528, 223 N.E.2d 869, 277 N.Y.S.2d 377 (1966); *Riviera Congress Assocs. v. Yassky*, 18 N.Y.2d 540, 223 N.E.2d 876, 277 N.Y.S.2d 386 (1966); see Reuschlein, *Limited Partner Derivative Suits*, 9 St. Mary's L.J. 443 (1978).

171. E.g., N.Y. Bus. Corp. Law § 626(b) (McKinney 1963); ABA-ALI Model. Bus. Corp. Act § 49 (1971). Section 1002 states: "In a derivative action, the plaintiff must be a partner at the time

for not having made a demand, be pleaded. Similarly, section 1004 specifies that a successful plaintiff is entitled to reimbursement of his legal expenses from the award and must remit the remainder to the limited partnership.¹⁷³

Unfortunately, the correspondence with corporation law in this article is incomplete. For instance, New York, like other states, has enacted a security-for-expenses statute pursuant to which plaintiff-shareholders with small holdings in a corporation can be compelled to post security to compensate the defendant-directors for their legal expenses should the suit prove groundless.¹⁷⁴ Although it is arguable that such statutes serve to discourage meritorious as well as unfounded suits, it would be anomalous to impose such a requirement as to shareholder derivative suits and not as to those involving limited partnerships. Accordingly, a security for expenses provision has been added to the New York limited partnership statute.¹⁷⁵ The new Act, however, fails to include a similar provision.

In addition, a large number of states,¹⁷⁶ including New York,¹⁷⁷ mandate indemnification of directors for litigation expenses incurred in the successful defense of shareholder derivative suits. The New York statute,¹⁷⁸ as well as the Federal Rules of Civil Procedure,¹⁷⁹ also require judicial approval of settlements in shareholder derivative actions. In both instances the new Limited Partnership Act fails to make similar provisions for general partners in the corresponding limited partnership derivative actions. Although the New York and Delaware statutes correct the deficiency in each case,¹⁸⁰ corresponding provisions in the new Act would have been desirable. At least the new Act could have suggested these as optional provisions for states having such corporate law sections.

CONCLUSION

The new ULPA is an improvement over the old Act in many respects. The 1916 Act was obviously deficient in its failure to deal with foreign limited partnerships, and its failure to specify the acts which subject a

of bringing the action and (1) at the time of the transaction of which he complains or (2) his status as a partner had devolved upon him by operation of law or pursuant to the terms of the partnership agreement from a person who was a partner at the time of the transaction." Allowing the derivative action to devolve pursuant to the terms of the partnership agreement seems more liberal than most corporate statutes.

172. N.Y. Bus. Corp. Law § 626(c) (McKinney 1963); H. Henn, *supra* note 2, § 367, at 774-75.

173. See N.Y. Bus. Corp. Law § 626(e) (McKinney 1963); H. Henn, *supra* note 2, §§ 373, 377.

174. N.Y. Bus. Corp. Law § 627 (McKinney Supp. 1978).

175. N.Y. Partnership Law § 115-b (McKinney Supp. 1978).

176. See H. Henn, *supra* note 2, § 380, at 804-13.

177. N.Y. Bus. Corp. Law §§ 721-27 (McKinney 1963 & Supp. 1978).

178. *Id.* § 626(d).

179. Fed. R. Civ. P. 23.1.

180. N.Y. Partnership Law §§ 115-c, 115-a(4) (McKinney Supp. 1978); Del. Code Ann. tit. 6, § 1732(d) (1974).

limited partner to personal liability for exercising an improper amount of control over partnership affairs. The new Act deals expressly with both matters, in its article on foreign limited partnerships (article 9), and in the provisions on control (section 303). Nevertheless, the treatment of both matters could be more adroit. For instance, the provision as to foreign limited partnerships is overly generous in allowing the foreign entities greater privileges than those organized locally. Conversely, the control provisions, perhaps because of an exaggerated fear of unfavorable tax consequences, probably do not go far enough in permitting limited partners to exercise control. Furthermore, the section could have been more specific than it is as to the effect of the statute on previously litigated control problems.

Recognizing that the limited partnership is an alternative to the corporation, especially for small business, the new Act borrows many corporate law provisions—for example, the extensive list of certificate and filing requirements which are similar to corporation statutes. If congruence with the corporate law is desirable, this desiderata of parallel provisions will necessitate widespread local amendment, thus sacrificing the virtue of national uniformity—a dilemma which it seems impossible to avoid.

Certain provisions of the new law represent dubious policy decisions; for example, those authorizing future services as consideration, and the loan and priority provisions. In many states, their adoption will cause an undesirable incongruity with the corporation statutes.

The prefatory note to the new Act states:

Articles 1 and 2 reflect an important change in the statutory scheme: recognition that the basic document in any partnership, including a limited partnership, is the partnership agreement. The certificate of limited partnership is not a constitutive document (except in the sense that it is a statutory prerequisite to the creation of the limited partnership), and merely reflects matters as to which creditors should be put on notice.¹⁸¹

Unfortunately, the draftsmanship of the new Act does not bear out this statement. The certificate seems to have a much greater significance, with serious potential liabilities for failure to amend, than the Note would indicate, and yet still is not sufficient without a separate agreement. This uneasy compromise between the functions of the two documents can only cause interpretive difficulties.

The same interpretive difficulties are true of many other provisions of the new Act. While certain improvements in specificity have been made in the sections treating dissolution, the complexity of the withdrawal, dissolution, winding up, and distribution provisions, despite their superficial clarity, will undoubtedly lead to interpretive difficulties. Judicial resolution of these problems will be necessary.

In short, while the new Act is better than the old one, it is not that much better. Legislators should, therefore, think twice about adopting it in its present form.

181. ULPA, Commissioners' Prefatory Note, (1976).